

E-002/CI-93-6; E-002/RP-93-630 ORDER ACCEPTING COMPANY'S PROPOSAL WITH  
MODIFICATIONS AND REQUIRING FURTHER FILINGS

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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In the Matter of an Investigation into  
Establishing a Bidding Process to Select  
Resources to Meet the Future Capacity Needs  
of Northern States Power Company

ISSUE DATE: August 18, 1994

DOCKET NO. E-002/CI-93-6

In the Matter of Northern States Power  
Company's Application for Resource Plan  
Approval 1994-2008

DOCKET NO. E-002/RP-93-630

ORDER ACCEPTING COMPANY'S  
PROPOSAL WITH MODIFICATIONS AND  
REQUIRING FURTHER FILINGS

**PROCEDURAL HISTORY**

In 1992 LS Power Corporation filed a complaint regarding the power purchasing practices of Northern States Power Company (NSP or the Company). Docket No. E-002/C-92-899.

During the course of the complaint proceeding, NSP indicated a desire to establish a bidding process to select the resources necessary for future additional capacity.

On January 12, 1993, the Commission issued its ORDER REQUIRING BIDDING PROPOSAL in the complaint docket. In that Order the Commission required NSP to develop and file a bidding proposal by February 1, 1993. The Commission attached a list of questions the Company was to address in its proposal. The Commission assigned the bidding proposal issues to Docket No. E-002/CI-93-6.

On February 1, 1993, NSP filed its bidding proposal. The Company proposed a supply-side bidding program under which new capacity, as well as the size and timing of resource additions, would be established through the Company's resource planning process. Most of the critical elements of the proposal would be included in a generic Request for Proposals (RFP), which the Company would submit as part of its resource plan.

On July 9, 1993, the Commission issued its ORDER REQUIRING FURTHER FILINGS REGARDING BIDDING PROPOSAL. In that Order the Commission directed NSP to file its generic RFP on July 30, 1993, in conjunction with its resource planning filing (Docket No. E-002/RP-93-630). The Commission also ordered the Company to submit a compliance filing addressing certain issues pertaining to the bidding process.

On July 30, 1993, NSP filed its generic RFP.

On August 23, 1993, NSP filed the compliance report addressing the bidding process.

On December 9, 1993, the Commission issued its ORDER CONSOLIDATING DOCKETS AND REQUIRING FURTHER FILINGS. In that Order the Commission found that the original distinctions between the bidding docket and the resource plan docket were no longer meaningful. The Commission decided that it would be best to consolidate the two dockets into one

proceeding. The Commission also ordered the Company and commenting parties to address certain questions regarding the bidding process.

On January 31, March 17, and March 31, 1994, response comments were filed by NSP.

During the course of the proceedings, the following parties filed comments: the Department of Public Service (the Department); the Residential Utilities Division of the Office of the Attorney General (RUD-OAG); Union of Concerned Scientists (UCS); the North Star Chapter Sierra Club; Minnesotans for an Energy-Efficient Economy; the City of Minneapolis; District Energy of St. Paul; Northern Natural Power, Inc. (Northern); the Izaak Walton (IWLA); the Minnesota Renewable Energy Society; the Wisconsin Public Service Commission (PSC); and the North Dakota Public Service Commission.

NSP's bidding proposal and generic RFP came before the Commission for consideration on June 1 and July 7, 1994.

## **FINDINGS AND CONCLUSIONS**

### **I. Introduction**

In this Order the Commission will first examine the issues surrounding NSP's proposed bidding process. The Commission will then describe the basic elements of NSP's proposed generic RFP. Finally, the Commission will analyze the main issues raised by the Company's proposed RFP.

### **II. The Bidding Proposal**

#### **A. Introduction**

The Commission agrees with the general consensus of the parties that NSP's bidding proposal is a reasonable step towards objective, open, efficient selection of the Company's resource options. The bidding proposal presents a reasonable means of identifying reliable, environmentally sound and least-cost generation sources for NSP as it faces future capacity needs. The bidding process, which incorporates the concept of an RFP tailored to individual capacity needs, is a means of applying objective selection criteria to assist the Company in its resource selection. The bidding process will also aid the Commission and other public agencies in their oversight of resource selection.

The Commission agrees with the Company's proposal, supported by other parties, to limit the bidding process to supply-side resources. As the Department stated in its March 3, 1993, comments, bidding should at least be limited to supply-side "until we gain more experience with the integration of demand- and supply-side resources in resource planning."

The Commission also agrees with the commenting parties that NSP should have the opportunity to compete as a bidder (so long as sufficient system safeguards are included). Opening the process to NSP, a knowledgeable and experienced bidder, can work to the advantage of ratepayers.

The Commission will comment in turn on the main issues surrounding NSP's bidding process.

#### **B. Commission Review and Oversight**

Commission review and oversight will consist of the following steps in the bidding process:

1. The Company will develop a list of approved evaluators, subject to input from all of the regulatory jurisdictions in which it provides service.
2. The Company will select an evaluator from the list approved by the public utility commissions in the various jurisdictions.
3. The Commission will review the Company's initial contract with the evaluator.
4. The Company will file its specific RFP with the Commission 60 days prior to issuing the RFP.
5. The evaluator's initial report and short list will be filed with the Commission, the Department, and the RUD-OAG at the same time it is served on the Company. The Department and the RUD-OAG may request an investigation within 15 days of receiving the report; the Commission may initiate an investigation within 30 days. If no investigation is initiated, the process will continue.
6. NSP will file the evaluator's final report and selection with the Commission, the Department, and the RUD-OAG at the time it announces its selection. If NSP does not select the bidder recommended by the evaluator, it will also file a detailed explanation of its selection. The Department and the RUD-OAG may request an investigation within 15 days of receiving the report. The Commission may initiate an investigation within 30 days of receiving the final report and selection.
7. The Commission will review and approve the final contract.

The parties generally supported the proposed process of Commission oversight and review. The Commission finds that the proposal provides sufficient opportunity for regulatory oversight, while retaining necessary flexibility in the bidding process.

There was some disagreement regarding the seventh element of Commission oversight, the Commission's review and approval of the final contract. The Department and the RUD-OAG maintained that the Commission should not approve the Company's contracts with the selected bidders. The agencies felt that this approval might limit the Commission's discretion to find the contracts imprudent in the Company's next rate case.

The Commission agrees with the Company that the Commission should review and approve the final contract in the bid selection process. As the Company conforms to the competitive bidding process, it should be able to rely on the Commission's approval of its contract with the selected bidder. If the Company later acts upon the contract in an imprudent fashion, the Commission retains the right to disallow rate case recovery of any resulting costs.

### **C. Two-Step Bid Process**

Both the IWLA and the UCS proposed a two-step bid process. Under the first part of this proposal, in which only renewables would be allowed to participate, the bid price would be capped by a proxy "avoided cost" for renewables. All renewable projects priced at or below the avoided cost would be accepted for contract negotiations. If unfilled capacity needs remained after this first step, a second, nonrenewable bid solicitation would take place. The IWLA and UCS felt that this proposal would ensure that all qualified renewable projects would be identified and considered.

The IWLA and UCS cited various reasons that cost-effective renewable resources might not win if they were subject to an all-source bidding competition rather than the two-step process. The reasons included the difficulty of evaluating intermittent renewable resources using standard

scoring procedures, and difficulties in quantifying the environmental benefits of renewables in all-source bidding.

The Commission agrees that there may be sufficient reason to develop a two-step bid process to ensure full consideration of renewables in the future. The Commission notes, however, that a significant number of renewable resources are already scheduled to come on line in the next two years. The Commission therefore finds that the issue of two-step bidding should be deferred to the Company's 1995 resource plan filing. The Commission will require NSP to address the issue of two-step bidding in that filing. All parties will then have the opportunity to comment on the proposal in the resource plan process.

#### **D. Renewable Set-Aside**

In its July 9, 1993, ORDER REQUIRING FURTHER FILINGS REGARDING BIDDING PROPOSAL, the Commission noted that 1993 legislation, codified as Minn. Stat. § 216B.2422, subd. 4 (1993 Supp.), requires Minnesota utilities in most cases to use renewable resources as the principal fuel in new or substantially modified electric generating facilities. The Commission found that separating, or setting aside, renewable resources into their own bidding cluster could be appropriate in certain circumstances.

In comments on the Company's 1993 resource plan, parties requested that the Commission order a renewable set-aside, or separate renewable RFP, in the resource plan.

The Commission finds that the issue of a renewable set-aside should be deferred to the Company's 1995 resource plan. An earlier renewables-only bid process should not be necessary, due to the heavy commitment to renewables already imposed by the Prairie Island legislation.<sup>1</sup> Also, as the Department notes, the Company's immediate plans call only for bids for peaking and wind resources; a renewables-only bid for peaking is not viable. For these reasons, the Commission will defer consideration of a renewable set-aside to NSP's 1995 resource plan filing.

#### **E. Renewable Preference**

As discussed previously, the Minnesota legislature established a renewable preference when it passed Minn. Stat. § 216B.2422, subd. 4 (1993 Supp.). Under that statute, the Commission may not approve a new or refurbished nonrenewable energy facility in an integrated resource plan unless the utility has demonstrated that a renewable energy facility is not in the public interest.

In order to monitor the competitive bidding process against the public interest standard, the Commission will need to know all renewable facilities that were evaluated, both in the initial evaluation and the final evaluation from the short list. The Commission will therefore require the Company to ensure that the evaluator has identified all renewable facilities that were evaluated, in both the evaluator's initial and final reports.

#### **F. NRG Energy, Inc. as a Bidder**

In the Commission's December 9, 1993, ORDER CONSOLIDATING DOCKETS AND REQUIRING FURTHER FILINGS, the Commission ordered NSP to specify the procedures it would use to ensure the confidentiality of bids, given the fact that it expected to participate as a bidder.

On January 31, 1994, the Company submitted a filing in which it stated that NSP-Generation would not participate in the bidding process. NSP would, however, participate through its

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<sup>1</sup> Minn. Laws 1994, Chapter 641 (SF 1706).

subsidiary, NRG Energy, Inc. (NRG), a Delaware corporation. NSP stated that its subsidiary would compete as an Exempt Wholesale Generator under the National Energy Policy Act of 1992.

NSP proposed a number of measures to ensure confidentiality in a bidding process in which NRG would participate. NRG would have access only to bidding information which was available to other bidders. When NRG submitted a bid to NSP, it would contemporaneously file the bid with the Commission. Employees of the subsidiary would not participate in any manner in the evaluation process, and negotiations between the subsidiary and parent would be confined to the written word.

The Department stated that the Company's proposed confidentiality measures, along with the structure of the bidding process itself, should help ensure arms' length participation by the subsidiary in the bidding process.

The Commission agrees that the Company has set out appropriate measures to protect the integrity of the bidding process. The Commission will add one procedure to ensure that the process is open and truly competitive. If NRG is selected to the evaluator's short list of bidders, the evaluator will be required to file the final report directly with the Commission. This is in contrast to the basic procedure, which contemplates the evaluator's filing the final report with the Company (which in turn files it with the Commission, the Department, and the RUD-OAG at the time of the final bid selection).

With these protective measures in place, the Commission will allow NRG to participate in the bidding process. If ratepayers are sufficiently protected, they may benefit from the participation of an experienced bidder of proven reliability.

### **G. Issues from the Lake Benton Bid Docket**

In August, 1993, NSP awarded a contract for the provision of 25 megawatts (MW) of wind capacity near Lake Benton, Minnesota. On March 29, 1994, the Commission denied a petition to open an investigation into the bidding process used in awarding the contract.<sup>2</sup>

Several issues arose in the Lake Benton docket which pertain to the Company's development of a bidding procedure. The issues of best and final offer and the provision of relative price ratings will be discussed later in this Order. Two other issues arose in the Lake Benton docket: the unilateral alteration of bid price; and the use of subjective criteria.

#### **1. The Unilateral Alteration of Bid Price**

In the Lake Benton bidding process, the independent evaluator unilaterally reduced the projected capacity output of Northern Natural Power's proposed facility and correspondingly increased Northern's bid price by 10%. Parties cited this issue, among others, in their request for an investigation of the bidding process.

The Commission notes that the evaluator may at times be required to exercise its expertise in determining the reliability of claims presented in a particular bid. The evaluator may decide that an adjustment in projected capacity levels is appropriate. In such a case, it should be the bidder, not the utility or the independent evaluator, that decides whether or not to adjust a bid price to reflect adjusted capacity levels.

In the NSP bidding procedure, the Commission will not allow bid price to be altered by the Company or the independent evaluator without consultation with and approval of the bidder.

#### **2. Subjective Criteria in Bid Selection**

In the Lake Benton bidding procedure, the evaluator's final report listed several subjective criteria in addition to objective RFP criteria. Although parties to the Lake Benton process did not claim that the contract was awarded on the basis of non-RFP criteria, the experience demonstrated the need for clearly articulated reasoning in the final selection.

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<sup>2</sup> In the Matter of the Request for an Inquiry into Northern States Power Company's Solicitation for Wind Power at Lake Benton, Minnesota, Docket No. E-002/M-93-1303, ORDER DENYING PETITION.

In the NSP bidding procedure, the Commission will require that the evaluator's initial and final reports clearly demonstrate why one bid was selected over others, based on the criteria in the approved RFP.

#### **H. Best and Final Offer**

The issue of best and final offers also arose in the context of the Lake Benton docket. Parties in that proceeding protested that bidders were not aware that there would be a request for a best and final offer, and that the low price was revealed at the time the best and final offer was requested.

In this docket NSP developed a model for the best and final offer (termed by NSP a final refined offer). The Company accepted certain modifications suggested by the Department and arrived at a best and final offer process as follows:

1. After completing all of the bid clarification meetings, the Company will request that each short-listed bidder submit, at the bidder's option, a final written refined offer.
2. Bidders submitting final refined offers may include proposed refinements that reflect insights gained through bid clarification meetings and/or reflect changes in fuel or financial market conditions that may have occurred since the original proposal was submitted to NSP.
3. The final refined offer is not intended to be a re-bid. If NSP or the independent evaluator believe that the final refined offer constitutes a new bid, the offer will be rejected.
4. Guidelines and restrictions on bid refinements will be defined in advance of short list announcements to allow this information to be provided to short-listed bidders concurrently with or soon after their announcement.
5. If an NSP affiliate is on the short list, the independent evaluator will audit NSP's request for final refined offers.

The Commission finds that NSP's final refined offer proposal adequately answers the issues raised in the Lake Benton docket. With the safeguards NSP has built into the process, the final refined offer should be an aid to selection of the best possible bid.



## **I. Equity or Purchased Power Adjustment**

In its comments NSP consistently argued that long term purchased power contracts create a financial obligation that increases the utility's business risk. Higher risk means that the utility must increase its percent of equity, which in turn increases the cost of purchased power. NSP asked the Commission to adopt its proposal for an equity adjustment to compensate for increased costs. In the alternative, NSP asked for contested case proceedings on this issue. NSP argued that a factual dispute exists among the parties regarding the need for an equity adjustment.

The Commission has addressed purchased power adjustment issues in several previous Orders. In the October 25, 1993, ORDER AFTER CONSIDERATION OF EVALUATIVE ISSUES IN SECTION 712 OF THE ENERGY POLICY ACT OF 1992, Docket No. E-999/CI-93-207, the Commission stated that issues of risk and price compensation would be dealt with through individual contract terms. The Commission stated that it would consider the effects of power contracts on a utility's financial position in the context of resource plan proceedings, competitive bidding dockets, and any other regulatory procedures in which long-term wholesale purchased power contracts are relevant.

In the Commission's November 13, 1992 Order approving and modifying NSP's 1991 resource plan, Docket No. E-002/RP-91-682, the Commission stated that decisions regarding equity adjustments should be made on a case-by-case basis.

The Commission remains convinced that decisions regarding possible equity adjustments should be made on a case-by-case basis if possible rather than through generic contested case proceedings. The individual nature of power purchase contracts requires individual consideration rather than a more general proceeding.

At this time, the Company does not have a power purchase contract before the Commission for consideration. The Commission will therefore not consider or decide the need for an equity adjustment at this time.

The Company is free to request an equity adjustment at the time it brings a power purchase contract to the Commission for approval. If the Commission deems the contract matter subject to a factual dispute, the Commission has the discretion to order a contested case if necessary.

The Company is also free to pursue recovery of an equity adjustment in contested rate case proceedings, should the Company believe that its aggregate power purchases require a contested case.

In either the request for contract approval or the rate proceeding, the Commission would be able to deal with the equity adjustment issue in the context of the surrounding factual circumstances.

The Commission will not adopt NSP's proposal for an equity adjustment, nor will the Commission grant the Company's request for contested case proceedings on this issue.

## **J. Size Threshold for Bidding Participation**

The Company proposed a threshold of 12 MW for competitive bidding. Any projects of 12 MW or more would be subject to the bidding procedure. The Department supported this figure.

The Commission agrees that 12 MW is an appropriate threshold for bidding requirements. This threshold ensures that major projects are subject to the open, competitive bidding formula. At the same time it is sufficiently high to allow small power producers needed flexibility to propose projects outside the bidding process.

The Commission agrees with the Company and the Department that further bidding experience will enable the Commission to either confirm the proposed threshold or adjust it if necessary.

#### **K. Use of the Competitive Bidding Process in 1994**

Because the Prairie Island legislation requires NSP to procure an additional 100 MW of wind capacity by December 31, 1996, NSP is planning to issue an RFP for an additional 100 MW of wind capacity this summer.

The parties have agreed that NSP's bidding process, though far from perfected, could be used to select the 100 MW of wind in 1994. NSP could also use an RFP for procurement of peaking capacity in 1994. Any elements in the RFP which are undeveloped or unclear should be subject to the discussion and settlement process described at Section III (C) of this Order.

The Commission believes that the issues arising regarding wind and peaking resource needs are sufficiently narrow and focused to be amenable to the developing bid process. Experience in bidding for these needs should be invaluable for the full development of the bid proposal.

#### **L. Evaluation and Continuing Refinement of the Bidding Process**

The competitive bidding process is a fairly new concept nationwide. NSP is the first Minnesota utility to bring a competitive bidding proposal before the Commission for approval. Selection of resources through the bidding process can have significant impact on rates, reliability of service, and the environment.

For all these reasons, the development of the bidding process has been closely watched by regulatory agencies, potential bidders, other utilities, and environmental groups. While parties are in general agreement regarding the major points of the proposal, it is also generally recognized that the NSP proposal will undergo change as it develops. As NSP stated in its comments, "[as it] gains experience with competitive bidding, proposal evaluation factors and the relative weighing of those factors are expected to evolve accordingly."

To assist the Commission's oversight of the developing bid process, the Commission will require the Company to file a formal evaluation. The evaluation should be submitted after completion of the first two competitive bids, but no later than July 1, 1995. The report should include a discussion of the successes and problems encountered with the bidding process, as well as suggestions for change.

In addition, the Commission encourages NSP to work with interested parties on a continuing basis to improve the competitive bidding process.

#### **M. The Relationship of PURPA to the Bidding Procedure**

Under the Public Utility Regulatory Policies Act (PURPA), utilities are required to purchase available capacity from a qualifying facility (QF) at the utility's avoided cost.

Under NSP's proposal, the Company would not be required to make capacity payments to QFs that provide offers outside the bidding process. According to NSP, requiring the Company to make capacity payments to non-bidding QFs would render the bidding process meaningless.

The Wisconsin PSC supported NSP's position.

At this time, the Commission is considering the Company's proposed competitive bidding process. Neither the Company nor the regulatory agencies have had the opportunity to see the process implemented in an actual bidding procedure. Although it is quite likely that NSP will

receive an unsolicited offer from a QF in future competitive bidding, such a fact situation is not now before the Commission. The Commission will therefore defer consideration of the relationship of PURPA payments to the bidding procedure until the fact situation is brought before the Commission. If a QF above 12 MW makes an offer for a project and requests capacity payments outside of a competitive bidding project, the Commission will decide if the Company is bound to make capacity payments to the QF.

The Commission will not accept the portion of the Company's proposal which eliminates capacity payments to nonbidding QFs. No decision will be made on this issue at this time.

### **III. The Proposed Generic RFP**

#### **A. Introduction**

Most parties found the major elements of the Company's generic RFP acceptable. The IWLA and RUD-OAG, however, felt that the proposal was too flawed to warrant implementation at this time.

Parties raised questions regarding NSP's proposal for weighing the three broad evaluation categories: price, project status and viability, and environmental impact. Parties raised concerns that NSP understates the importance of environmental factors. The Department recommended that, to the extent possible, environmental factors be considered directly in the price score.

Both the IWLA and RUD-OAG had concerns regarding the non-price factors. The IWLA questioned if the allocation of non-price points reflects the value of the non-price points to ratepayers. The RUD-OAG felt that there is too much weight allocated to non-price factors. Heavily weighing such criteria as risk could tip resource selection toward existing traditional sources rather than promising new ones.

The IWLA and RUD-OAG recommended that the Company perform further testing of the bid process before implementing any actual bids. Other parties stated that the generic RFP, though less than perfect, is sufficiently developed to allow the Company to begin bidding. Further refinements can best be made with the benefit of actual experience.

#### **B. Elements of the Generic RFP**

NSP's proposed generic RFP contains six main elements: 1) Introduction and overview; 2) Scope of work; 3) Instructions to bidders; 4) Proposal threshold requirements; 5) Response package; and 6) Proposal scoring worksheet.

##### **1. Introduction and Overview**

This section introduces the prospective bidder to what generation resource(s) NSP is looking for and provides an overview of the bidding process that will be used. Because NSP's resource needs will vary among specific RFPs, the generic RFP provides only a list of items that might typically be included.

##### **2. Scope of Work**

NSP anticipates that the scope of work could vary among specific RFPs as technology advances and transmission system and generating facility operating practices evolve. The generic RFP therefore provides only a list of typical scope of work items, such as generating facility project development, interconnection boundaries, project siting, construction, and operational permitting and regulatory compliance.

### **3. Instructions to Bidders**

This section provides the bidder with specific instructions regarding the submission of proposals in response to the RFP. The section also describes the proposal evaluation process in detail.

### **4. Threshold Requirements**

This section communicates to bidders the minimum acceptable technical, commercial, and financial requirements of a proposal submitted in response to an NSP RFP.

### **5. Response Package**

This section provides specific instructions to bidders regarding proposal format. The instructions would include such items as General Instructions, Public Disclosure Summary, Project Proposal Description, and Bidding Tables.

### **6. Proposal Scoring Worksheet**

The Proposal Scoring Worksheet is actually an especially important element of the Response Package. This section shows bidders the specific evaluation criteria and methodology that will be used to score proposals. Through use of the worksheet, bidders will be able to estimate roughly the non-price portions of their proposal scores.

## **C. Report on the Generic RFP**

Most parties agreed that the generic RFP is sufficiently developed to allow the Company to proceed with bidding for its current wind and peaking needs. Parties, including NSP, also agreed that issues remain outstanding and that further development of the generic RFP will be necessary.

The Commission notes with approval that parties have filed constructive comments throughout this proceeding and that NSP has responded to parties' comments as the generic RFP has been shaped. The Commission will require interested parties to meet further to discuss the remaining issues relating to the generic RFP. The Commission will require the Company to file a report on the parties' discussions within 90 days of the date of this Order. The report should include but not be limited to a discussion of the following topics:

1. A proposal to test selection criteria to determine the appropriate allocation of price and non-price points.
2. A proposal to score price on a linear basis.
3. A specific proposal for a method of integrating the Commission's interim environmental cost values into the price score.
4. Revision or justification for the maximum score threshold at 30 percent equity.
5. Criteria for judging the quality of the project financial plan.
6. A proposal for modeling optimal combinations of bids.

Two other topics should be explored in the compliance report: compliance with the standard form contract; and the role and use of environmental cost.

### **1. Compliance with the Standard Form Contract**

Under NSP's proposed generic RFP, one threshold requirement is a bidder's agreement to "substantially comply" with NSP's standard power purchase contract terms and conditions. If a bid proposal does not meet the threshold requirements, it will be rejected.

Northern argued that the term "substantial compliance" was not defined in the Company's RFP. The concept of substantial compliance made negotiations with the Company difficult, since any degree of deviation from the standard contract posed the possibility of rejection. Northern also argued that a carefully drawn generic RFP and standard form contract should supply the necessary requirements which bidders must meet.

The Commission finds that Northern has raised concerns regarding this issue which should be addressed by NSP. The Commission will therefore require the Company to discuss the threshold requirement of substantial compliance with a standard form contract in its 90-day compliance filing.

## **2. Role and Use of Environmental Costs**

NSP proposed adding the Commission's values for environmental costs to project price to determine price points. Most parties agreed that this proposal is consistent with Minn. Stat. § 216B.2422, subd. 3(a) (1993 Supp.), which requires utilities to use the environmental cost values set by the Commission when evaluating and selecting resource options in proceedings before the Commission.

Issues remained regarding the Company's application of the environmental values. The Company proposed using a single value. The Department advocated using the midpoint of the range selected by the Commission. The RUD-OAG opposed the use of any single value, stating that this may be inconsistent with the statutory concept of value ranges.

The Commission agrees that environmental values must be selected and applied carefully. The use of a range of values was deliberately set by statute to allow the Commission to exercise some discretion and also to implicitly consider nonquantified socioeconomic impacts. The value range also reflects the fact that environmental values are not precisely quantifiable.

The Commission will require the Company to include the parties' discussion of the application of environmental costs in the bid process in their 90-day compliance filing.

### **D. A Limit on Front-Load Security**

In its original proposal, NSP defined front-loading as any situation where the present value of the capacity charge in a year exceeds the present value of all capacity charges, divided by the number of years. Under this definition, if a project featured levelized capacity charges, the provider would be required to pay significant front load security for several years.

Responding to concerns expressed by the IWLA, the Company modified its method of computing front-loading. Under NSP's current proposal, the present value of the annual capacity payment is now compared with an actual levelized annual capacity payment. This method results in a lower front-load security requirement and eliminates the need for front-load security for projects featuring a levelized payment stream.

While the Commission finds that NSP's present method of calculating front-load security is appropriate, one further element may be advisable in certain cases. Under some circumstances, an absolute limit on front-loading may be a prudent measure to limit ratepayer risk. The Commission will therefore require the Company to review the issue of a front-loading limit on a case-by-case basis in specific RFPs.

## **E. Price Points**

### **1. Relative Price Scoring**

NSP's proposed price scoring mechanism is relative. Relative price scoring assigns the lowest bidder the top score; all other bidders are scored in relation to the lowest bidder. A relative scoring method creates a non-linear price function: changes in price that are of the same magnitude will cause changes in price scores of different magnitudes, depending on the baseline.

The IWLA opposed the use of relative scoring because it believed that relative price scoring distorts the worth of price and non-price factors. A non-viable project with a low price could actually alter the rankings of other viable projects, potentially resulting in the selection of a less than optimal proposal. The IWLA also believed that relative scoring prevents bidders from optimizing bids. A bidder cannot calculate its price score (or relative aspects of its non-price score) or estimate how an increase in cost incurred to increase its non-price score will affect its price score. The IWLA suggested that these problems could be solved by creating an absolute scoring mechanism, based on the utility's avoided cost for the project.

The Commission believes that the IWLA has raised a valid concern regarding the Company's relative price scoring mechanism. While the inability of bidders to self-score and optimize bids arguably may not be harmful, the distortion of price and non-price factors could clearly result in an unsatisfactory selection of resources. The Commission finds that the Company should explore methods of scoring price proposals on a linear basis. A linear scoring function should solve the potential problem of distortion raised by the IWLA.

The Commission recognizes that development of a linear price scoring method may take some time, as the Company gains experience and refines the bidding process. Until a linear method is developed and approved, the Commission will require the Company to adopt an interim method which will address the problems inherent in the Company's current pricing method.

The Commission will require the Company to rerank all bids on the short list if the low-priced bid does not receive enough points to make the short list. Under this method, the lowest bid on the short list would receive the maximum 600 points, and all other short-listed bids would be scored in relation to that bid. The Commission also recommends that NSP rerank the top one or two bidders who did not make the short list, to make sure that they were not excluded as the result of the non-viable low bid. This method of reranking bids should preserve the relative distribution of points while ensuring that the bidding does not produce a non-optimal resource selection.

In the meantime, the Company should also continue to develop a linear price scoring mechanism.

### **2. Revelation of Price Rating**

In the Lake Benton bid process, when the Company requested short-listed bidders to submit best and final offers, each bidder had enough information to calculate what the initial low bid was. In the current proposal, the Company would also reveal the low bid, although it would not necessarily reveal price points before all final offers were at hand. NSP stated that revealing the price points and the low bid would demonstrate that the selection process was fair.

The RUD-OAG argued that the Company's transmission of bid information could harm the bid process in a number of ways: it could discourage participation by disadvantaging the bidder in other bids, establish a false price, and discriminate against the lowest bidder.

The Commission finds that the RUD-OAG has raised valid concerns. Development of a linear price scoring mechanism will render the issue moot, since the low bid's price could not then be calculated from another bidder's price points. Until the linear method is developed, the Commission will require the Company to refrain from revealing information which would permit parties to calculate any price offered in the bid. At the least, the Company should not reveal price points at the time the short list is released.

### **3. Escalation Starting Values, Heat Rates, and Sensitivity Analyses**

The Wisconsin PSC recommended that starting values should be specified for escalation rates, that projects using escalation should specify a heat rate, and that an analysis of sensitivity to different escalation rates should be required if escalation rates are used.

NSP did not respond to the Wisconsin PSC's recommendations regarding starting values, heat rates, or sensitivity analyses.

The Commission finds that the Wisconsin PSC's recommendations are reasonable and useful. The Commission will require that these provisions be adopted in NSP's bidding proposal.

### **F. Non-Price Points**

In its bidding proposal, NSP designated ranges and criteria within factor scores to give direction to the evaluator on how non-price points should be awarded. The bid proposals would not be scored in relation to each other but rather according to how well they ranked according to the specified criteria.

The Commission finds that NSP's approach to scoring on non-price points is appropriate.

The Commission agrees with one change suggested by the IWLA. The Project Schedule and Milestones category should be evaluated according to how many hurdles to project implementation remain, rather than according to the number of hurdles crossed. This approach will help to select the most viable project.

## **IV. Remaining Issues**

The Commission also approves the elements of the Company's bidding proposal not covered in this Order.

### **ORDER**

1. The Commission accepts the Company's bid proposal as modified in this Order.
2. The Company shall address the issue of a two-step renewable bid process in its 1995 resource plan.
3. The Commission denies the Company's proposal for an equity adjustment, and the Company's alternative request for a contested case proceeding on this issue.
4. On or before July 1, 1995, the Company shall file a report evaluating its experience with the bidding process.
5. Within 90 days of the date of this Order the Company shall file a report outlining issues discussed with interested parties, as described in Section III (C) of this Order.

6. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar  
Executive Secretary

(S E A L)